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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1969

No. 282

UNITED STATES OF AMERICA,
Petitioner,

vs.

MACLIN P. DAVIS and EDITH U. DAVIS,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

PETITION FOR REHEARING

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SUPREME COURT OF THE UNITED STATES

No. 282. — October Term, 1969

UNITED STATES, Petitioner, v. **MACLIN P. DAVIS et ux.**	**On Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit.**

PETITION FOR REHEARING

TO THE HONORABLE CHIEF JUSTICE AND ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES

MAY IT PLEASE THE COURT:

Maclin P. Davis and wife, Edith U. Davis, respondents in the above case, respectfully petition the Court for a rehearing of the decision and judgment of March 23, 1970, remanding the case to the District Court for dismissal of the complaint. As in the opinion of the Court, Maclin P. Davis will be referred to as "taxpayer."

In the opinion of Mr. Justice Marshall, concurred in by four members of the Court, no mention whatever is made of taxpayer's fundamental contention (the first one made in his brief) that a return of capital is not "income" within the Sixteenth Amendment. The Court states in the opinion (p. 11) that "the difference between form and substance in the tax law is largely problematical." But on a constitutional issue, the problem must be squarely faced. We respectfully refer the Court to the discussion at pp. 3-6 of the reply brief, and to the quotation from *Eisner v. Macomber*, 252 U. S. 189, 206, in which this Court stated that the determination of what is and what is not "income" must

be "according to truth and substance, without regard to form." It is clearly within the competence of Congress, in making exceptions to the taxation of true income, to prescribe the form which must be followed by the taxpayer to take advantage of the exception. But, as stated by the Court in *Eisner v. Macomber*, it is not within the competence of Congress to "conclude the matter" of what is income by any test other than truth and substance.

The attribution rules are not truth and substance, but pure fiction, if applied to determine what is "income" within the Sixteenth Amendment. Moreover, the Court has apparently assumed that the sole owner of preferred stock and common stock of a corporation is affected in exactly the same way by the redemption of his preferred stock as by the redemption of a part of his common stock. Ownership of property is a bundle of rights (and privileges), and where a part of the common stock is redeemed, the sole stockholder's bundle is the same as before the redemption, except for the smaller number of shares, which is form and not substance. But the redemption of his preferred stock changes the bundle materially, because preferred stock is not fungible with common stock. Preferred stock can be, and in this case was, clearly earmarked as property separate and distinct from the common stock. Only in the complete liquidation of a corporation does the difference between preferred stock and common stock lose significance.

The rationale of the Court's decision is such that if a stockholder buys preferred stock one day, and sells it the very next day for the same money he paid for it (or even for the cancellation of a note given for it), the sales price is taxable income to the extent of the corporation's earnings and profits, provided only that, either in fact or by application of the attribution rules, the seller is the sole stockholder. We submit that no semantic legerdemain can justify such a fiction, which flies in the face of any concept of income "according to truth and substance." We continue to urge that Congress intended no such result. One purpose of Section 302(b)(1) of the Internal Revenue Code of 1954 was doubtless to provide a safety valve to save the constitutionality of the 1954 revision. But we respectfully submit that if the Court's conclu-

sion as to the meaning (or lack of meaning) of Section 302(b)(1) be accepted, the taxing statute is rendered clearly unconstitutional, because the result is to tax as income what is really a return of capital.[1]

Respectfully submitted,

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[1] Although this petition is predicated on the constitutional issue, we feel compelled also to challenge the Court's statement that if a transaction failed to qualify under Section 302(b)(2) or (3) solely because of the attribution rules "it would *according to taxpayer's argument* nonetheless qualify under Section 302(b)(1)." (Emphasis supplied.) Taxpayer's argument, to the contrary, is simply that such redemptions as are returns of capital would so qualify. The redemption of stock issued to the taxpayer as a stock dividend is an obvious example of a redemption which is not a return of capital.

CERTIFICATE

The foregoing petition for rehearing is presented in good faith and not for delay.

ROBERT G. MCCULLOUGH
WILLIAM WALLER

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SUPREME COURT OF THE UNITED STATES

No. 282.—October Term, 1969

United States, Petitioner, v. Maclin P. Davis et ux. | On Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit.

[March 23, 1970]

Mr. Justice Marshall delivered the opinion of the Court.

In 1945, taxpayer and E. B. Bradley organized a corporation.[1] In exchange for property transferred to the new company, Bradley received 500 shares of common stock, and taxpayer and his wife similarly each received 250 such shares. Shortly thereafter, taxpayer made an additional contribution to the corporation, purchasing 1,000 shares of preferred stock at a par value of $25 per share.

The purpose of this latter transaction was to increase the company's working capital and thereby to qualify for a loan previously negotiated through the Reconstruction Finance Corporation. It was understood that the corporation would redeem the preferred stock when the RFC loan had been repaid. Although in the interim taxpayer bought Bradley's 500 shares and divided them between his son and daughter, the total capitalization of the company remained the same until 1963. That year, after the loan was fully repaid and in accordance with the original understanding, the company redeemed taxpayer's preferred stock.

[1] References in this opinion to "taxpayer" are to Maclin P. Davis. His wife is a party solely because joint returns were filed for the year in question.